

California Debt and Investment Advisory Commission

LIVING WITH AN ISSUE: ON-GOING DEBT ADMINISTRATION SEMINAR

April 19-20, 2007

The following information contains answers for a few questions that did not get asked during the April 19-20, 2007 CDIAC seminar, "Living with an Issue: On-going Debt Administration" seminar. Question cards were distributed to the class and collected at the end of the program.

The answers to the lingering questions are provided by Peter Shapiro, Managing Director, Swap Financial Group LLC and Keith Norris, Manager of Treasury and Debt Management, from the Metropolitan Water District of Southern California.

Q-Card: How are Swap advisors paid? On a fixed basis? By whom?

Norris - It is up to you. You can pay them on a negotiated fixed fee basis, or pay them through the price of a swap (typically in basis points). We have paid them directly through invoice payments.

Shapiro - The most common method is to pay the swap advisor out of the swap – i.e. to embed the advisory fee in the swap, and thus have the rate you are paying on the swap (generally, that is the fixed rate) be adjusted slightly higher to account for the fact the swap is shouldering the cost of the advisory fee. Typically, fees embedded in a swap raise the rate by one to five basis points (depending on the size and duration of the swap). Alternatively, you can pay a fixed fee directly to the swap advisor, but in our experience, only a minority of clients do this. Either method is totally acceptable, however.

Q-Card: Is it better for an entity to have a Swap Advisor for all Swap transactions or better on a deal by deal basis?

Norris - Again, up to you. We retain our swap advisors on a contract basis, and compensate them through hourly fees and transaction costs. We have also used multiple swap advisors.

Shapiro - We generally think that best practice is to have a swap advisor for all transactions, though practice does vary. The advantage in having a single, consistent advisor is that they tend to have a better feel for your needs and practices over time, and they get to know your history and hot button issues better. We think there's a genuine value for the client in continuity in advisory relationships. There are two other practices: Some clients hire an advisor for a single transaction, and once the transaction is over, they may never call for the advisor's services again. The disadvantage is the swaps are long-term two-way commitments, and it's often better to have an advisor "on call", to help monitor and evaluate possible changes. The other practice among certain very active swap users is to use multiple advisors, and to alternate which one to use. This is fine for big, sophisticated clients, but is less applicable for the rest of the universe.

Q-Card: If you want to refund a transaction that has a Swap, how easy or difficult is it to unwind the Swap or roll the Swap to the refunding?

Norris - Depends, if you are still in the escrow period, more problematic with the tax attorneys if the escrow period is still in effect, not sure if you can even do it. If the escrow period is over, then you have the option to continue to "use" the prior swap with the new transaction, or as always you can terminate the swap at your preference. If the prior transaction does not have an escrow, then you can always terminate the swap, or keep it one. Best to discuss this matter with your tax attorneys.

Shapiro - Generally, this is doable, a swap can be associated with any of a number of transactions. If the underlying bonds are to be refunded, it is generally possible to transfer the swap to a new set of bonds, or to terminate the swap and take into account the termination payments received or made in the new refunding transactions. It's important to have good lawyers on this, and all bond counsel are not equally adept at understanding the nuance of the law, especially because the isn't very clear. A good swap advisor will generally have seen many permutations of this type of transaction, and be a valued member of the team in analyzing alternatives.